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The Manufacturers Hanover
Financial Digest
Weekly Commentary, Selected Financial Data, and Business Indicators

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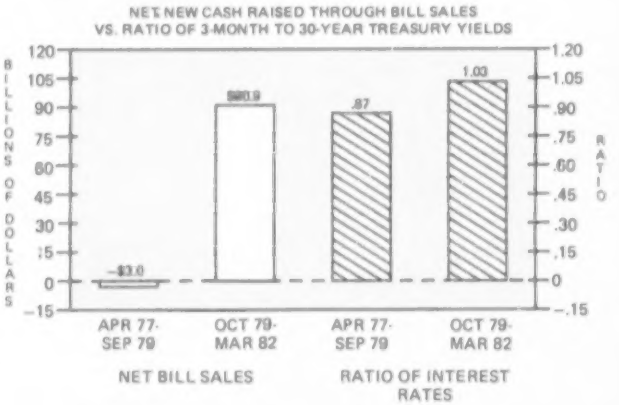
A Shift From Bills To Bonds . . .

One of the least attractive—though not unexpected—by-products of the Federal Reserve's emphasis on controlling the growth of the supply of money rather than its price has been severe interest rate instability. At a time of record credit demands and monetary restraint, volatile short-term interest rates have plagued all financial market participants—not to mention contributing to the lofty interest rate structure now in place. As a consequence, borrowers and lenders alike have converged in the short end of the debt markets—the former to avoid locking in costly long-term funds, and the latter to seek the more attractive yields prevailing in the money markets. But in so doing, a Catch-22 has emerged: with short-term borrowings surging in hopes of future interest rate declines, rates have done precisely the opposite. They remain high, thus perpetuating bond market disarray and causing yet additional short-term borrowing.

While the increasing reliance on short-term debt by the private sector has received widespread attention, that of the Federal government has not. But just as corporations and now, state and local governments have turned increasingly to short-term finance since the Fed's de-emphasis of interest rate stability in October, 1979 so, too, have the Treasury's debt managers—further clogging the already overcrowded short-term debt markets.

During the ten calendar quarters beginning October 1, 1979 and ending March 31, 1982, almost 40 per cent, or $90 billion, of net new cash raised by the Treasury was derived through sales of three, six and twelve-month bills. By contrast, during the ten calendar quarters prior to October, 1979—when a total of $72 billion of net new cash was raised—there was actually a net paydown of Treasury bills outstanding. Thus, not only has the volume of short-term debt issuance soared, so has its relative importance.

Although increased bill sales may provide greater debt management flexibility, they have also contributed to the virtual disappearance of the positive yield differential between short- and long-term debt. Whereas three-month bill yields stood at about 85 per cent of 30-year bond rates, on average, during the ten quarters prior to October, 1979, short yields averaged approximately 105 per cent of bond rates during the subsequent ten quarters. As a consequence, bond market investors found it was no longer rewarding to commit funds long-term. Rather, short-term investors reaped the highest returns (see chart).



. . . May Be Just What The Doctor Ordered

Thus it can be seen that, not only has the growing volume of Treasury finance contributed to financial market volatility, but so, too, has the pattern of debt issuance. If true, the outlook is bleak. Unless present restrictions now barring new bond issuance are lifted, the Treasury will have to rely even more on shorter-term finance. Net borrowings are likely to approach $50 billion in the third quarter of this year, of which almost half may be raised through bill sales. Both would be new record highs, raising the possibility of higher short-term interest rates and a very short-lived economic recovery—if, indeed, one gets underway at all.

One way to unclog the money markets would be for Washington to aggressively step up its long-term debt sales. True, this means that Washington will be locking in costly, and noncallable, long-term funds. But it could have salutary side effects. For if the Treasury had limited bill sales in this fiscal year to only ten per cent of net new cash to be raised,

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short-term borrowings would drop by an astonishing $50 billion—not far from the total size of the nonfinancial corporate commercial paper market! What is more, even this proportion of funds raised would be high by historical standards; in fiscal years 1978 and 1979, for example, bill finance accounted for less than two per cent of net new cash raised.

Diminished short-term Federal borrowings would encourage the reemergence of a positively-sloped yield curve—inducing investors to once again lengthen the maturity structure of their assets. As more cash flows into longer-term instruments, corporations would benefit by being able to fund their short-term liabilities in the long-term markets, paying down short-term debt while securing sorely needed long-term investment finance. Even the battered thrift industry could benefit. With their cost of funds falling relative to both mortgage lending rates and yields prevailing on existing assets, the thrifts might turn profitable again at best, or at least slow the hemorrhage of red ink, at worst.

Convertibles May Take . . .

Although the statistics coming from Detroit are still gloomy, there is a glimmer of hope on the horizon. Sales of domestic automobiles have perked up from a low of five million units at an annual rate at the end of April to a 6.2 million pace for the last 40 selling days. Inventories at manufacturers' plants and dealers' lots were pared to only 52 days' sales on June 1—one of the lowest levels in recent years.

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 6/9/82	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	138.709	– .237	+11.091
Loans to Depository Inst.	1.306	+ .254	– .899
Float	2.472	+ .029	– 1.179
Total Reserve Bank Credit	151.004	– .230	+ 8.113
Treasury Deposits with Federal Reserve Banks	3.409	+ .571	+ .796
Currency Outside Banks	130.928	+ .623	+ 8.158
Member Bank Reserves:			
Required	38.405	– .527	– .870
Excess (Deficiency)	.150	– .542	– .072
Total Reserves Held	38.555	– 1.069	– .942
Net Borrowed Reserves	.939	+ .839	– .767
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	92.535	+ 1.500	– 4.875

Monetary Aggregates†		% Change Since Three Months Ago*	% Change Since Year Ago
M1	454.4	+ 4.4‡	+ 5.6‡
M2 (May '82)	1,894.7	+ 10.2	+ 9.4
M3 (May '82)	2,275.4	+ 11.0	+ 10.2
L (January '82)	2,659.1	+ 9.1	+ 10.9

†Seasonally adjusted. *Seasonally adjusted annual rate. ‡Four-week moving average.

New York Money Market

Offering Rates 6/18/82	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	12.50%	12.95%	12.80%
* Federal Agencies	13.40	13.65	14.10
* Project Notes—Taxfree (46% Taxable Equivalent)	14.07	15.00	NA
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	15.10	15.20	15.40

‡Finance Company Paper—Prime

5- 14 days	13.50%
15- 29 days	14.13
30- 59 days	14.25
60- 89 days	14.13
90-179 days	13.63
180-239 days	12.88
240-270 days	12.00

‡* Bankers' Acceptances

Jul.	14.30%
Aug.	14.40
Sep.	14.40
Oct.	14.40
Nov.	14.25
Dec.	14.00

‡Industrial Paper—Prime

30- 89 days	14.15%
90-120 days	14.15

†Federal Funds Effective Rate 14.13%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	1st Q'82	$ 2,992	$ 2,998	$ 2,853
Gross National Product (1972 Dollars)*	1st Q'82	$ 1,482	$ 1,498	$ 1,516
Percent Change, Annual Rate	1st Q'82	– 4.3	– 4.5	8.6
Change in Consumer Prices (all urban consumers)*	Apr '82	2.4%	– 3.6%	4.8%
Change in Producer Prices*	May '82	0.0%	1.2%	2.4%
Civilian Employment (Thousands of Persons)†	May '82	100,117	99,340	101,045
Unemployment as % of Civilian Labor Force†	May '82	9.5%	9.4%	7.5%
Personal Income*	May '82n	$ 2,548	$ 2,532	$ 2,367
Leading Indicators Composite Index (1967=100)†	Apr '82	125.2	124.2	137.3
Industrial Production Index (1967=100) †	May '82n	140.3	140.6	152.7
Net Change in Consumer Installment Credit†	Apr '82	$ 1.18	$ 0.99	$ 2.72
U.S. Merchandise Trade Balance †	Apr '82	–$ 0.32	–$ 2.64	–$ 3.48
Plant and Equipment Expenditures*	3rd Q'82	$328.04(a)	$336.77(a)	$328.25
Private Housing Starts (Thousands of Units)*	May '82n	1,086	888	1,172
New Construction Expenditures*	Apr '82	$ 232.8	$ 234.2	$ 246.5
Total Business Inventories†	Apr '82	$ 508.5	$ 507.6	$ 487.1
Total Business Sales†	Apr '82	$ 339.9	$ 343.1	$ 350.9

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. a-Anticipated.

Demand for a few models has actually outpaced production, keeping them in very short supply.

However, a glance at consumers' balance sheets suggests that car sales should have picked up at a much faster pace. People have curtailed their borrowing in the aftermath of the 1980 credit controls, real incomes have increased as inflation has slowed and household liquid assets are at record levels. This extra purchasing power has not been directed into homes or housing related areas, leaving replacement of aging autos a likely step. The average age of cars now on the road is about seven years—the highest in over 30 years.

What is more, other indicators, which have been traditionally important determinants of future car sales have turned positive. The cost of operating and maintaining a car (including monthly car payments, gasoline, repairs and insurance) has been declining since last December and is now only 2.1 per cent higher than a year ago. Finally, the differential between new and used car prices has narrowed significantly, which in the past signaled a revival in new car sales. What, then, has kept the lid on sales?

. . . The Lid Off Car Sales

It seems that in the scramble for fuel economy, downsized American cars have become underpowered, overpriced and boring. While most people may no longer be interested in making a statement

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Negotiable Time CD's Weekly Reporting Banks			
Nationwide (6/2/82)	135,919	– 142	+16,735
New York City (6/2/82)	33,359	– 734	+ 4,996
Commercial Paper (6/2/82)	176,222	+ 118	+35,880

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (6/2/82)	209,058	+ 794	+31,926
New York City (6/2/82)	58,927	+ 249	+ 6,777

Total Loans Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (6/2/82)	486,088	+ 3,113	+48,305
New York City (6/2/82)	114,121	+ 1,379	+ 8,350

Financial Markets

	Friday 6/18/82	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	13.26%	+ .64	– 1.91
180-Day Bills†	14.20	+ 1.00	– .94
Longest Bills†	14.48	+ .92	– .14
Recent Issues:			
14³/₈s 6/30/84 (When Issued)	14.92	NA	
14s 3/31/86	14.73	+ .59	
13³/₄s 5/15/92	14.69	+ .68	
14s 11/15/11	14.18	+ .52	
Municipals:			
Bond Buyer–20 Bond Index* (6/17/82)	12.63%	+ .23	+ 1.90
Blue List Total ($ Million)	$1,009	– $ 48	– $ 90
30-Day Visible Supply ($ Million)	$2,168	– $686	– $ 86
Total	$3,177	– $734	– $176
Corporates:			
Moody's Aa Composite (6/17/82)	15.29%	+ .16	+ 1.08
30-Day Visible Supply ($ Million) ‡	$1,375	– $630	NA
Stocks:			
Dow-Jones Averages:			
Industrials	788.62	– 21.12	– 207.57
Transportation	305.01	– 13.49	– 115.22
Utilities	106.70	– 3.26	– 3.56
65 Stocks	306.78	– 9.87	– 78.16
Standard and Poor's 500 Stocks	107.28	– 3.96	– 24.69
N.Y.S.E. Composite Index	61.74	– 2.20	– 15.01
N.Y.S.E. Avg. Daily Vol. for Week (000's)	48,928	– 4,546	– 5,518

* 46% Taxable equivalent 23.39%.
‡ Series redefined: Historical data not available.
† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 6/18/82	Week Ago
Overnight	14.25%	14.00%
1 month	15.38	14.31
3 month	16.13	14.75
6 month	16.25	14.94
1 year	16.13	15.00
EURODOLLAR BONDS Average Yield		
Medium Term (5 to 7 yrs.)	15.15%	14.65%
Long Term (7 to 15 yrs.)	15.00	14.75

FOREIGN EXCHANGE SPOT RATES

New York Opening (6/18/82)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02125	47.06
Canada	.7738	1.2924
Denmark	.1182	8 4585
France	.1470	6.8025
Germany	.4072	2.4558
Italy	.0007249	1379.50
Japan	.003917	255.30
Mexico	.02095	47.74
Netherlands	.3693	2.7075
Switzerland	.4723	2.1175
U.K.	1.7355	.5762

about themselves by the car they drive, they still want an attractive car at a reasonable price. Two recent examples of such a combination are selling so well that several plants have been running overtime. Production of the new Chevrolet Camaro is 50 per cent higher so far this year than a year ago while sales last month were almost triple those of May, 1981. Output of Pontiac's Firebird is 85 per cent ahead of a year ago while sales last month have more than doubled from last year. The revival of the convertible has also been successful, especially for Chrysler's "K" line.

On the other hand, the increased availability of gasoline at a lower price has prompted a resurgence of interest in some larger models, too. Purchasers of U.S.-made vehicles still apparently prefer to buy by the pound—much to the consternation of domestic producers—believing that a larger car has more value. Furthermore, the older-style models are more attractively priced, since their production costs have long been amortized. This contrasts with the steep retooling costs that manufacturers incurred for the compacts and subcompacts designed since 1979. ■

GOLF FANS' DREAM WEEK

WHAT:
The Manufacturers Hanover Westchester Classic

WHERE:
Westchester Country Club, Harrison, New York
From New York City on the New England Thruway: Exit 20. From Connecticut: Exit 21. On the Cross Westchester Thruway, East: Exit 10

WHEN:
Mcnday, June 21, thru Sunday, June 27
Monday: Qualifying Round; Tuesday: Practice Round and Junior Golf Day; Wednesday: Pro-Am; Thursday: First Round; Friday: Second Round; Saturday: Third Round; Sunday: Final Round

WHO:
Many of the top pros on the PGA TOUR—
including Ray Floyd, defending champion—competing for $400,000 in prize money. Winner's purse: $72,000

HOW:
Tickets available at the gate and at all branches of Manufacturers Hanover in Westchester County
Sports House and Grounds: $60 for all 7 days; $5 each day for Monday and Tuesday; $10 for Wednesday; $15 each day for Thursday, Friday, Saturday and Sunday

Grounds only: $40 for all 7 days; $3 each day for Monday and Tuesday; $6 for Wednesday; $12 each day for Thursday, Friday, Saturday and Sunday

Youngsters 14 and under, accompanied by an adult: $5 (at the gate only)

WHY:
The opportunity to see championship golf and support the 11 Westchester hospitals that share in the proceeds

For ticket information, call 914-967-5386

SEE YOU THERE!

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